

**CABINET
15 SEPTEMBER 2020**

**DELIVERY OF NEW HOMES AT NEASHAM ROAD
JOINT VENTURE PROPOSAL AND LAND DISPOSAL**

**Responsible Cabinet Member –
Councillor Alan Marshall, Economy Portfolio
Councillor Charles Johnson, Resources Portfolio
Councillor Kevin Nicholson, Health and Housing Portfolio**

**Responsible Director –
Paul Wildsmith, Managing Director
Ian Williams, Director of Economic Growth and Neighbourhood Services**

SUMMARY REPORT

Purpose of the Report

1. To update Members on the proposed delivery of new homes on Neasham Road.
2. To approve the establishment of a new Joint Venture Company (JVC) between Esh Homes Ltd and Darlington Borough Council which will provide the infrastructure to open the site and then build and sell homes on parts of the site, as shown at **Appendix 1**.
3. To seek approval from Members on the proposed disposal terms of land agreed between the Council and the new JVC.
4. To seek approval for the Council to build 150 Council owned affordable homes on the site and determine the Sustainable Code Level which the dwellings are to be built to.
5. To seek approval from Members to utilise the £2.8m Housing Infrastructure Funding (HIF) for strategic infrastructure at Neasham Road.

Summary

6. The Council issued an OJEU procurement exercise in Summer 2017 to seek a joint venture partner for residential development. Esh Homes Limited were appointed following that exercise. This partnership has already proved to be a successful model for the accelerated delivery and provision of housing within the Borough and the delivery of income for the council via profits and loan interest payable.
7. At the meeting of Cabinet on 6 March 2018, the Council approved the acquisition of land at Neasham Road with the overall objective of providing circa 450 new homes which included the provision of 300 affordable homes.

8. This approval was subsequently followed with a further report to Cabinet on the 8 January 2019 at which members approved the disposal of land at Neasham Road, to the JVC. It was also agreed that a report on the agreed terms for the disposal of this land would be brought back to Cabinet for final agreement.
9. Subject to the acquisition of land within the site, to be acquired by compulsory purchase powers (CPO) and vacant possession of the former allotments, it is proposed the Council will dispose of Part A to the new JVC and Part B to be used for the development of Council owned affordable homes. It is currently proposed that Part C would be sold to a Registered Provider or retained by the Council for Council owned affordable homes. The JVC would provide strategic infrastructure to the whole site and costs apportioned between the parties.
10. A planning application for the whole site was submitted in March 2020. This application was presented to the Council's Planning Committee on 5 August 2020 where planning approval was granted.
11. In summary the application was granted for the development of 449 homes, as shown on the Plan at Appendix 1. These are divided into three parts;
 - (a) Part A – JVC development for the provision of 155 privately owned homes
 - (b) Part B – Council owned affordable housing development for 150 homes and:
 - (c) Part C – (outline planning) for 144 homes to a Registered Provider or Council owned affordable homes.
12. It is again important to acknowledge that the acquisition of the land at Neasham Road provides an opportunity for much needed social and affordable housing development but this acquisition was part of a wider strategy presenting several key benefits.
 - (a) Facilitates the relocation of the cattle mart operation from a site close to the town centre to a new purpose-built facility on the outskirts of town capable of delivering a new agricultural cluster.
 - (b) Allows the inclusion of the cattle mart site to be a part of the multi-million-pound regeneration investment into Bank Top station area and in time will deliver a capital receipt for disposal of Clifton Road.
 - (c) Facilitated accelerated build out at Stag House farm through the JVC and Barratts together with the £2.8m HIF grant funding from Homes England, that can be recycled through this development.
 - (d) The site would act as a significant contributor to the Councils identified need for social housing.

Recommendation

13. It is recommended that Cabinet: -
 - (a) Approve the establishment of a new JVC to deliver, build and sell new homes at Neasham Road and delegate authority to the Assistant Director Law and Governance to finalise the negotiations for the establishment of the JVC.

- (b) Approve £8.5m from the Investment Fund to fund the JVC financed by prudential borrowing subject to a legal charge in favour of the Council over the Land acquired by the JVC company together with a Guarantee from the Joint Venture partner in respect of 50% of the loan sum.
- (c) Approve the sale of the land to the JVC, conditional upon the completion of the Joint Venture Agreement.
- (d) Authorise the Assistant Director Law and Governance to execute the sale of the land, the entering into the joint venture and associated documents accordingly.
- (e) Authorise the Assistant Director of Resources, the Assistant Director Housing and Building Services and the Assistant Director Law and Governance are appointed to act as directors in the JVC as part of its Executive Board.
- (f) Approve that upon completion of the Joint Venture agreement that a secured loan facility be entered into with the JVC as a secured loan simultaneous with the land transaction.
- (g) Approve that Area A is developed by the JVC and allocate Area B to the Council's new build affordable housing scheme on the terms and conditions outlined in Part III of this report at **Appendix 2a and at Appendix 2b**, and agree that the Director of Economic Growth and Neighbourhood Services be granted Delegated Authority to finalise negotiations in line with the terms reported.
- (h) Agree to give delegated powers to the Director of Economic Growth and Neighbourhood Services to transfer the land at Area B to the HRA, in line with the terms outlined in Part III of this report at **Appendix 3** and provide 150 Council owned affordable homes at an estimated build cost of £24.13m for Sustainable Code 3 level plus financial contributions towards s106 costs, and works undertaken by the JVC, or an additional cost of £14,000 per property for 150 dwellings for Code 4. Details of the Section 106 obligations are outlined in Part III of this report at **Appendix 4**.
- (i) Approve the termination of agreements relating to the former allotment land to secure vacant possession and negotiate compensation as appropriate.
- (j) Agree to release funding required to facilitate the development and to fund the additional fees, development costs and annual maintenance costs in relation to ecology, on the terms and conditions outlined in Part III of this report see **Appendices 2a, 2b and 3** and to use the £2.8m HIF funding currently utilised on Stag House Farm on strategic infrastructure at Neasham Road . The external funding and commercial envelope information relating to Neasham Road is identified in Part III of this report at **Appendix 5**.

Reasons

14. The recommendations are supported by the following reasons: -

- (a) To contribute to the our Covid recovery in line with the agreed Economic Strategy.

- (b) Accelerates the building of new homes for sale by the JVC and contributes to our much-needed social housing requirement.

Paul Wildsmith
Managing Director

Ian Williams
Director of Economic Growth
and Neighbourhood Services

Background Papers

Appendices as listed below:

- i. Appendix 1 – Site Plan showing Area A, B and C.
- ii. Appendix 2a and 2b Part III report – Development Appraisal and Heads of terms for the disposal to the JVC.
- iii. Appendix 3 Part III report – Heads of terms for the Council owned affordable housing development
- iv. Appendix 4 Part III report – Section 106 obligations
- v. Appendix 5 Part III report – Commercial Envelope
- vi. Appendix 6 Part III report – Reserved Matters

Guy Metcalfe: extension 6725

S17 Crime and Disorder	This report has no implications for crime and disorder
Health and Well Being	There are no Health and Well Being Issues
Carbon Impact	There are no sustainability issues
Diversity	There are no diversity issues
Wards Affected	Hurworth
Groups Affected	Not Applicable
Budget and Policy Framework	This report does not represent a change to the budget and policy framework
Key Decision	This is not a key decision
Urgent Decision	This is not an urgent decision
One Darlington: Perfectly Placed	There are no issues adversely affecting the Community Strategy
Efficiency	An investment return from the JV will help the Council's MTFP position.
Impact on Looked After Children and Care Leavers	Looked after Children and Care Leavers could benefit from the Council's affordable housing units not least of all because one is planned to be a Children's home

MAIN REPORT

Information and Analysis

15. The Council's established JVC's have already proved to be a successful model for the accelerated delivery and provision of housing within the borough. Details of the arrangements are outlined in this report and Shareholder Reserved Matters are outlined in Part III of the report at **Appendix 6**. With planning permission now approved the scheme will provide for 150 new Council owned affordable homes to be constructed and 155 open market homes by the JVC.

16. Detailed planning permission has been granted with outline planning approval also granted in respect of the middle area of land, area C, that is earmarked for development by a Registered Provider or the Council for circa 144 homes Council owned affordable homes as shown on the plan at Appendix 1.
17. Prior to build commencing there are still several issues to resolve:-
 - (a) Members are aware that a final land parcel acquisition through compulsory purchase powers is ongoing. In the event objections are received, an update will be reported back to Members for consideration at a future meeting.
 - (b) Demolition of two empty properties are required to facilitate the development and this is being undertaken by the Council using framework contracts.
 - (c) A small part of the site, former allotments land is used for grazing purposes and work is underway to seek vacant possession of these areas.
 - (d) In accordance with the planning approval some additional off-site ecology works are needed.

Land Disposals

18. The JVC will develop Area A as shown in the plan at Appendix 1 and will also procure enabling infrastructure to open and provide infrastructure for the wider site. This is a similar arrangement to the one adopted at Stag House. The heads of terms of the proposed disposal to the JVC are set out at Appendix 2a and 2b to be reported in Part III of this report.
19. It is intended the sale to the JVC would be completed once the CPO has been confirmed and concluded.
20. In order to ensure that ecology on the site is protected, works will not take place during March and September, so it is proposed some tree protection works are undertaken prior to these dates.
21. The enabling infrastructure works will be undertaken by the JVC and include highways works and sustainable drainage for the site.
22. The Council will develop Area B on the plan at Appendix 1. The heads of terms of the proposed disposal are set out at Appendix 3 to be reported in Part III of this report.
23. Area C on the plan at Appendix 1 will be retained by the Council and it is currently proposed would be sold directly to a Registered Provider or may be a future Council owned affordable housing development.
24. In accordance with the planning permission the Section 106 Agreement obligations will cover the whole site. Further details are given in Appendix 4 to be reported in Part III of this report.

The Council's New Build Affordable Housing Programme

25. The proposal is for the Council to build 150 units of affordable housing for rent comprising of:-
 - (a) 50x two bedroomed apartments
 - (b) 28x two bedroomed houses
 - (c) 50x three bedroomed houses
 - (d) 21x four bedroomed houses
 - (e) 1x five bedroomed house
26. The Strategic Housing Market Assessment identified that there is a need for 160 affordable dwellings for rent across the Borough of Darlington each year and other Registered Providers operating in the area provide relatively low numbers of affordable housing units on average.
27. Not only is there a need to build affordable dwellings to meet local need, it is also a business need for the Housing Service. The Business Plan is underpinned by the rents received from Council properties and the loss of rents as a result of previous regeneration works and ongoing right to buy sales significantly reduces income for the Housing Service if these properties were not replaced.
28. Now that the HRA borrowing cap has been abolished we are able to prudentially borrow additional resources to supplement the funding available from revenue contributions to capital. The Housing Business Plan approved by Council in March 2020 identified around £81m available to spend on new build in total going forward and with projected Homes England grant of £27m. In respect of the site at Neasham Road we have already secured £5.85m of HE grant funding and a further bid is pending for an additional £1.5m.
29. The cost of the Council's build works is anticipated to be £24.13m. The cost of works is based on anticipated tender prices. Full details of the costs of the overall requirements including infrastructure costs and planning requirements are provided at Appendix 3. It should be noted however that the overall costs are significantly higher than normal due to several factors including:-
 - (a) Significant landscaping and ecology treatment, as well as, play provision for the overall site being included in these costs
 - (b) Infrastructure costs and external works are much higher, reflecting the location of the site and include S278 works on the Highway
 - (c) Need for raft foundations and retaining walls
30. Members have also requested that consideration should also be given to whether this scheme should include additional sustainability measures to reflect the Council's commitment towards the Climate Change agenda. A range of measures have been identified to bring the properties to Sustainable Code 4, such as, Solar PV, air source heat pumps and improved insulation but further more detailed work would be required to agree the most appropriate measures, particularly taking into account feedback from tenants where these measures have been used previously. Meanwhile it has been estimated there would be an additional cost of £14k per property, adding a further circa £2.1m to the overall cost and bringing the total

scheme cost from £24.13m to £26.24m plus the s106, plus financial contributions towards s106 costs, land and works undertaken by the JVC.

The JVC Proposal

31. The proposal is to develop the part of the Neasham Road site under the Joint Venture arrangement; the benefits of this over a straightforward land sale to a single or multiple development are:-
 - (a) A share for the Council in developers' profits
 - (b) The Council retains more control over the overall site
 - (c) All infrastructure works are undertaken by the JVC therefore ensuring quality and delivery on time
 - (d) The arrangement gives greater flexibility
 - (e) The land value is negotiated to deliver value for money for the Council

The principles of the JVC are as follows

32. The Council enters into a disposal of the land with the JVC and into a loan facility agreement of up to £8.5m, simultaneously with security over the land and formal completion of the Joint Venture documents and a deed of guarantee from the Joint Venture Partner. The projected gross interest payable to the Council under the Loan Agreement is projected to be £1.265m.
33. The JVC contracts with building contractors in respect of the substantive works. All contracts with a value over £25,000 require the approval of the Council and it is a requirement that any contracted works comply with public procurement requirements and the Councils own requirements.
34. Total cost of the JVC development works is anticipated to be £27.5m. The cost of works is based on anticipated tender prices which are best value and are subject to validation by an independent Quantity Surveyor.
35. After the finance costs (payable to the Council and the Joint Venture Company), costs of sale and professional costs, the pre-tax profit to each partner is estimated at £1.1m.
36. Rate of return for the Council of circa 35% over the five-year scheme which is the expected build out period.
37. The Joint Venture agreement has the following heads of terms:-
 - (a) The JVC will deliver strategic infrastructure works, highways, drainage, SUDS and services as referred to in the Appendix 2b in Part III of the report.
 - (b) The Council will fund the project and investment and capital will be repaid to the Council over the life of the project.

- (c) The number of homes built at any one time is limited to reduce risks associated with sales.
- (d) The maximum funding requested is £8.5m.
- (e) Each joint venture partner will nominate three directors to the Executive Board.
- (f) Decisions made by the Executive Board by simple majority will be binding on all partners save as to the shareholder reserved matters which must be agreed by both shareholders in writing.
- (g) A process to resolve disputes is included.
- (h) The Joint Venture will incur costs and execute sales in accordance with the appraisal. Sales may not be made at less than 95% of the appraisal value without the consent in writing of both shareholders.
- (i) Profits will be shared equally (50:50) between the Joint Venture members.
- (j) The Agreement can be terminated under defined circumstances.
- (k) The Building contracts can be delayed or terminated under defined circumstances.

38. The principal elements of the Loan Agreement are:-

- (a) A cash advance by the Council to the JVC in the sum of up to £8.25m to fund the Joint Venture development.
- (b) Interest on the loan to be calculated at the State Aid compliant rate, currently 4.75% and variable over the term.
- (c) Security on the land to the extent of the advanced sum.
- (d) Legal Charge over the land to secure the lending.
- (e) The whole of the advance will be repayable as a debt if any instalment is not paid or in the event of any insolvency action.

39. The principal elements of the Building contracts are:-

- (a) Contract between JVC and building Contractor.
- (b) Based on formal tenders for the works.
- (c) Variations over £50,000 require consent in writing of the Council and Esh Homes Limited.
- (d) Works can be delayed at the instance of the JVC with agreed delay costs of £5,000 per week.

- (e) Terminable by the JVC on notice with agreed termination payment for demobilisation costs of £25,000.

40. The proposal is set out in the Appendices see the appraisal at **Appendix 2a**.

Risks Analysis and Valuation Comment

41. There are two main areas of risk on the expected return; *the cost of the build* (which if it increases will diminish profit) and the *achievement of the sales value*. Safeguards are in place on both elements as below.

Cost of Build

42. The expected total cost of the build contract is £27.1m. The Council's contribution to the build cost is restricted at any time to the amount of the loan advance.
43. Over the course of a building project the building contracts allow for required variation instructions to be given in the form of Architects Instructions (AIs). Increases to the building contract costs affect the profitability of the Council investment. Accordingly, the AIs are managed in two ways:-
- (a) Mechanism in the Building contracts that no AI or variation with a value in excess of £15,000 can be made without the approval in writing of the contract administrator.
 - (b) Mechanism on the Joint Venture Agreement that no variation with a value in excess of £15,000 can be made by the JVC save with the consent in writing of both the Council and Esh Homes Limited.
 - (c) Mechanism in the Joint Venture that the building contracts cannot be varied with cumulative variations with a total value in excess of £50,000 save with the consent in writing of both the Council and Esh Homes Limited. This will be recorded in the Joint Venture and in the Articles of Association of the JVC as a shareholders reserved matter as appended at Appendix 6.
 - (d) A further mechanism in the building contracts provides that the works are released on a staged basis of five units at a time. These phased releases are to be approved by monthly governance meetings and the requirement for this is recorded in the Joint Venture. The approval for further releases shall not be given where the sales programme is behind targets to the extent that the JVC does not have sufficient funds to meet the liability of the additional release.
 - (e) The Joint Venture Agreement governs the situation where consent is sought to sell properties for less than 5% below the appraisal value, or where the sales programme is behind the projections in the cash flows requiring a further advance on the loan agreement to maintain liquidity of the JVC. In such a case (on a case by case basis) the parties will not continue with the building contracts unless there is agreement in writing by both parties to do so. The parties may alternatively agree to delay the progress of the building contracts until the sales programme less than five units.
 - (f) The building contracts contains express provision that delay payments of £5,000 per week are incurred for delay at the request of the JVC. The contract

further makes provision to be terminated subject to a liability to the contractor of £25,000 being the contractually agreed termination costs for the building agreement which would be the contractual liability of the JVC to the Contractor in the event that further releases of the programme are not agreed under the mechanism outlined in para 28(e).

44. In such an event the Joint Venture agreement would be subject to the dispute resolution procedure and terminable.

Financial Implications

45. The works undertaken by the JVC are to provide enabling infrastructure to the whole of the site and it should be noted that the cost of these works exceeds the land receipt that would be expected from the JVC for Part A of the site. As such a reconciliation payment will be made by the Council to the JVC. Any works done for example, ecology works, in advance of the Joint Venture Company completing the sale in March 2021 will need to be done at risk and funded upfront by the Council. These works would be required in any event to facilitate development.
46. The Council will pay for their percentage share of the enabling infrastructure costs incurred by the JVC for the Council owned affordable housing site B and for the remaining site C. Site C will then be available for sale as a full enabled site. It is expected that an increased capital receipt will be received for this land from the future purchaser.
47. In the longer term it is anticipated that adjacent private land holdings may be brought forward for development with access gained from the infrastructure provided by this development. We anticipate further financial receipts as a result of this released development value with access gained from the Neasham Road development site.
48. Details of the commercial envelope for the whole site are given in Appendix 5 to be reported in Part III of this report.

Mitigation of Risk regarding the JVC

49. The Council's contributions are made to the JVC by shareholder lending supported by shareholder guarantee. The advance from the Council will be on the basis of the required state aid compliant interest rate required by the relevant EU legal communication notice. This is currently calculated at 4.75% per annum which equates to 4% plus the current UK base rate. The scheme length and scheduled repayment dates are set out in the Cashflows.
50. The Council's lending is proposed to be secured by a legal charge on the land and build and a restriction on title as well as the guarantee for 50% of the lending from the Joint Venture partner.
51. In addition to the safeguard above the funds at the bank will be protected as follows:-
- (a) Both of the Joint Venture members directors will be named on the company bank mandate have immediate direct access to account information.

- (b) Each of the Joint Venture members, ie Esh Homes Limited and the Council will cross guarantee to the other over the conduct of the bank account by their employee directors in the Joint Venture Agreement.
52. The Joint Venture Agreement governs the situation where consent is sought to sell properties for less than 5% below the appraisal value, or where the sales programme is more than five units behind the projections in the cash flows.
53. In such a case (on a case by case basis) the parties will not continue with the Building contracts unless there is agreement in writing by both parties to do so. The parties may alternatively agree to delay the progress of the Building contracts. A further mechanism in the building contracts provides that the works are released on a staged basis of five units at a time. These phased releases are to be approved by monthly governance meetings and the requirement for this is recorded in the JV. The approval for further releases shall not be given where the sales programme is more than five units behind the target shown in the cash flows.
54. The Building Contracts contain express provision that delay payments of £5,000 per week are incurred for delay at the request of the JVC. The contract further makes provision to be terminated subject to a liability to the contractor of £25,000 being the contractually agreed termination costs for the Building contracts which would be the contractual liability of the JVC to the Contractor in the event that further releases of the programme are not agreed.
55. In such an event the Joint Venture Agreement would be subject to the dispute resolution procedure and terminable with the interests and liabilities of each member calculated at that point.
56. The Joint Venture will operate on a risk reward basis, and each parties risk share will be limited to half of the required lending to fund the scheme.
57. The risk of non-payment of lending will be secured firstly against the land and assets of the JVC, as well as by a guarantee from the Joint Venture Partner for their share of the project.
58. Additionally, the building contracts will be let on flexible terms to ensure that they can be terminated early if needed and offering the Joint Venture Partners the opportunity to slow or phase development as needed to reflect changes in the market.

Outcome of Consultations

59. Internal consultations with Housing, Estates, Finance, Legal and Corporate Procurement have not raised any objections to the proposal.
60. Statutory consultation was carried out through the required planning process. These were taken into account during at the Council's Planning Committee.

Legal Advice

61. The Localism Act 2011 includes a 'general power of competence' which gives local authorities the legal capacity to do anything that an individual can do that is not specifically prohibited.
62. The Joint Venture is to be delivered with the Joint Venture partner appointed following an OJEU tender process conducted in Summer 2017.
63. Under the provisions of the Local Government Act 1999 the Council is subject to a general duty to obtain 'best value' in the exercise of its functions. Cabinet should consider in making the recommendations of this report that the deal represents value for money which is supported by obtaining independent valuation comment on the terms of the land disposal the Council's professional appraisal of the sales values and by requiring that the engagement of the building contract be conducted in accordance with tendering processes on an arm's length basis in accordance with the Council's own tendering thresholds.
64. Specific legal advice has been obtained on the envisaged agreements and the Assistant Director, Law and Governance, will be required to document the Joint Venture on the basis set out in this report, specifically in the Joint Venture Agreement, the Loan Agreement, the Legal Charge, the Deed of Guarantee and register the necessary restrictions at the Land Registry to protect the Council's interest in the scheme and mitigate any investment risk.